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TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: May 22, 2003

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Dear Sir or Madam:

We have considered the ruling request dated January 24, 2003, submitted on behalf of M by its attorney, relating to the tax consequences of the expanded activities of M.

FACTS

M was incorporated a number of years ago in the State of N on a nonprofit basis. M is exempt from federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code. It has also been classified as a public charity within the meaning of sections 509(a)(1) and 170(b)(1)(A)(vi).

M is an organization that focuses solely on offering advanced continuing education and training for professionals from all O departments, and from O-owned new Q-operations. M also offers at least two programs annually for P educators. These are designed, like M's other programs, to help educators stay abreast of the issues affecting Q industry professionals so that they can more effectively educate their students.

From its very beginning, M has focused its efforts on the sharing and discussion of Q industry "best practices." This was important to the professionals attending M programs because most Os were owned by individuals or families, and instruction among the professionals was limited. Through the seminars arranged by M, independent owners of Os

were offered the opportunity to meet or to send their employees to meet other O professionals to learn what practices they were using, as well as which practices were successful and which were not.

In the past, M began offering programs ("On-Site Programs") at its current headquarters in N. The On-Site Programs continue to offer attendees the opportunity to meet with other O professionals to discuss the issues they face in their profession. During the On-Site Programs, usually running for five days, the participants are given learning opportunities that combine specific course materials, presentations by guest discussion leaders, and small and large group discussion sessions, as well as a variety of social interactions in less formal settings. Because of its reputation for exceptional program content, and because its ultimate aim is to improve the quality of the Q industry's products and services, M is able to attract leading Q industry professionals and practitioners in other professions, government officials, and educators who contribute their time to serve as guest speakers and discussion leaders.

Participants are expected to complete any assigned reading or other assigned activities before attending the programs. Many programs offer attendees the opportunity to submit issues that they want to discuss at these programs, and then the programs are tailored to address these issues. Many programs also provide attendees with the opportunity to submit specific work products for critique by both presenters and other attendees in advance of the seminar.

A cooperative learning experience with a seminar structure is emphasized at the programs, "as contrasted to the theory-based instruction of colleges and universities with more broadly based, introductory courses on P, management, business, finance, legal and technical aspects of the O industry." It is M's experience that this type of instruction challenges and motivates the experienced Q industry professional.

M's seminars are open to all individuals in the Q industry. However, because its programs include advance level training in specialized areas, M provides guidelines on who should attend each seminar.

The need to adapt to changing conditions in the Q industry has forced M to more effectively tailor its On-Site Program to address the need for specialized training, and also to offer instruction through off-site means, whether through "live" instruction or distance learning. This growing shift in the method of delivering M's curriculum is the subject of this ruling request.

A significant change is the offering of information to Q industry professionals and the general public at M's website. The website not only allows M to provide on-line information about the programs and activities it offers, but also to provide instant access to up-to-date information on a continuous basis to Q professionals in a convenient and time-saving electronic format.

Individuals may subscribe to monthly electronic newsletters on M's website. One newsletter is R, which focuses on critical issues and trends in the Q industry, and the other is S, which contains a collection of insights and ideas from M staff members and other O professionals. M offers free electronic subscription to these newsletters simply by providing

name and e-mail address information for electronic delivery. Also, these newsletters are available to both O professionals and members of the general public.

Another feature of M's website is a forum program, whereby individuals can post and respond to messages relating to numerous topics. You have cited sample subjects discussed. There are also forums that focus on specific areas for O professionals, including forums for individuals who are involved with specialized areas in the Q industry.

A second change M has made is that it now offers programs at sites other than its corporate offices ("Off-Site Programs"). Currently, these Off-Site Programs include those where attendees are hosted and sponsored by a domestic or foreign Q organization. Generally, these programs are open only to professionals employed by the host organization. M saves costs in not having to rent space at an off-site location, has ready access to the facilities and technology it requires for instruction, and is assured of an appropriate class experience and sufficient class size.

When conducting these Off-Site Programs, M only rarely offers the host organization the option of offering existing programs from M's published curriculum. Instead, M ordinarily works with the organization to develop a new program. M retains all rights in any such tailored program so that it can be used elsewhere.

Initially, M and its Board were concerned that this form of program might compromise the integrity of the curriculum or instruction, or would not reach a sufficiently wide population. However, this has not proven to be the case.

The Off-Site Programs continue to evolve from existing M programming and are subject to the same quality control and review. Also, by offering tailored programs, M is given the opportunity to stay on the cutting edge of issues faced by Q professionals. Further, it allows M to educate those professionals in a more efficient manner. M takes the information it learns during its programs back to its staff for review and inclusion in future programs.

The Off-Site Programs have also enabled M to extend its impact to the improvement of the Q industry outside the U.S. The program offered leadership and skills training developed through decades of M's work with Q industry professionals. Other Off-Site Programs have been utilized by Scandinavian, Asian, African, and South and Central American Q industry professionals.

Although attendance at the Off-Site Programs is limited to employees of the host company, these programs normally reach a larger audience than the On-Site Programs. Thus, you inform us that, "In a recent Off-Site Program hosted by an organization that owns more than 100 Os, the attendees included representatives from approximately 115 different Os ... Generally, On-Site Programs attract attendees from approximately 15 to 30 Os. With greater numbers of Os represented..., attendees are exposed to an even greater number of information sources, different perspectives and issues to discuss and debate."

Many of the Q industry professionals who receive training in the Off-Site Programs are subsequently invited to share their expertise by being guest discussion leaders at M's On-Site seminars. You state that this sharing reflects M's longstanding role as a facilitator for discussion of "best practices" within the Q industry. The general public is the ultimate beneficiary of this ongoing discussion because of the improved performance of the participating Os.

RULINGS REQUESTED

1. The tailored programming, both on-site and off-site, as described above, is a charitable and educational activity, and, as such, does not jeopardize M's tax exempt status under section 501(c)(3) of the Code.

2. The income derived from the activities described above is related to M's exempt purposes, and, as such, will not result in the imposition of unrelated business income tax under section 511 of the Code.

LAW

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated "exclusively" for religious, charitable, educational, or other specified exempt purposes, "no part of the net earnings of which inures to the benefit of any private shareholder or individual," and which does not engage in proscribed lobbying and political activities.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in Code section 501(c)(3) in its generally accepted legal sense, and includes the advancement of education.

Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term "educational" includes the instruction or training of the individual for the purpose of improving or developing his capabilities or the instruction of the public on subjects useful to the individual and beneficial to the community. Example (2) is an organization whose activities consist of presenting public discussion groups, forums, panels, lectures, or other similar programs.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish such purposes. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. Thus, in construing the meaning of the phrase "exclusively for educational purposes" in Better Business Bureau v. United States, 236 U.S. 279 (1945), 1945 C.B. 375, the Supreme Court of the United States stated, "This plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes."

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a

private interest. Thus, an organization must establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 511 of the Code imposes a tax on the unrelated business taxable income (defined in section 512) of organizations exempt from tax under section 501(c).

Section 512(a)(1) of the Code defines the term "unrelated business taxable income" to mean the gross income derived by any organization from any unrelated trade or business (defined in section 513) regularly carried on by it, less the allowable deductions which are directly connected with the carrying on of such trade or business, both computed with the modifications provided in subsection (b).

Section 513(a) of the Code provides that the term "unrelated trade or business" means, in the case of any organization subject to the tax imposed by section 511, any trade or business the conduct of which is not substantially related to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption.

Section 513(c) of the Code provides that the term "trade or business" includes any activity which is carried on for the production of income from the sale of goods or the performance of services.

Section 1.513-1(a) of the regulations provides that gross income of an exempt organization subject to the tax imposed by section 511 of the Code is includible in the computation of unrelated business taxable income if: (1) it is income from a trade or business; (2) such trade or business is regularly carried on by the organization; and (3) the conduct of such trade or business is not substantially related (other than through the production of funds) to the organization's performance of its exempt functions.

Section 1.513-1(d)(2) of the regulations provides that a trade or business is "related" to exempt purposes only where the conduct of the business activities has a causal relationship to the achievement of exempt purposes (other than through the production of income). Further, it is "substantially related," for purposes of section 513 of the Code, only if the causal relationship is a substantial one. For this relationship to exist, the production or the performance of the service from which the gross income is derived must contribute importantly to the accomplishment of exempt purposes. Whether the activities productive of gross income contribute importantly to such purposes depends, in each case, upon the facts and circumstances involved.

Rev. Rul. 74-16, 1974-1 C.B. 126, holds that a nonprofit organization that provides instruction and training to individuals in foreign countries to enable them to organize and manage credit unions is an "educational organization" within the meaning of Code section 501(c)(3) and qualifies for tax exemption under this section.

Rev. Rul. 71-460, 1971-2 C.B. 231, holds that a domestic corporation that conducts part or all of its activities in a foreign country is not precluded from being recognized as tax exempt under section 501(c)(3) of the Code.

Rev. Rul. 68-504, 1968-2 C.B. 211, describes an organization formed to conduct an educational program for bank employees in a particular urban area. The organization described in the Rev. Rul. furnishes classrooms and employs local university professors and specialists in banking law to teach courses on various banking subjects. Membership in the organization is open to employees of all banks in the area. Citing section 1.501(c)(3)-1(d)(3) of the regulations, the Rev. Rul. concludes that the organization qualifies for exemption as an organization described in section 501(c)(3) of the Code.

Rev. Rul. 65-298, 1965-2 C.B. 163, describes a nonprofit organization formed for the purpose of carrying on research as to diseases and other disorders of the human body and to develop scientific methods for diagnosis, prevention, and treatment thereof. The organization then disseminated the results of such research to other physicians and the general public through seminars. The seminars are presented in various cities using, as speakers, teachers from medical schools and outstanding specialists in private practice. All results of this research (including any derivative patents, copyrights, processes, or formulas) are made available to the general public on a nondiscriminatory basis. The revenue ruling concludes that the organization is engaged in an educational activity within the meaning of section 1.501(c)(3)-1(d)(3) of the regulations because the seminars and lectures which it presents relate to the instruction or training of physicians for the purpose of improving and developing their capabilities. Held, the organization qualifies for tax exemption under section 501(c)(3) of the Code.

ANALYSIS

In order for M to continue to meet the requirements for recognition of exemption as an organization described in section 501(c)(3) of the Code, it must be organized and operated exclusively for charitable and educational purposes. Under section 1.501(c)(3)-1(c)(1) of the regulations, M must engage primarily in activities that accomplish such charitable and educational purposes, and no more than an insubstantial part of its activities may not be in furtherance of an exempt purpose. Also, in accordance with section 1.501(c)(3)-1(d)(1)(ii), M must not be organized or operated for the benefit of private interests.

As noted previously, section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" includes the advancement of education, and section 1.501(c)(3)-1(d)(3) defines "educational" to include the instruction or training of individuals to improve or develop their capabilities. As an illustration, Rev. Rul. 65-298, cited above, holds that an organization that sponsors seminars and lectures for medical professionals to assist them in improving their professional capabilities qualifies as an educational organization under section 501(c)(3) of the Code. Similarly, M's On-Site and Off-Site Programs are designed to improve and develop the leadership abilities and technical skills of Q industry professionals. In Rev. Rul. 68-504, cited above, the organization's conducting of an educational program for bank employees in a particular urban area was held to be educational where membership in the organization was open to employees of all banks in the area. Similarly, M offers its programs to both the general

public and professionals employed by host organizations. All such programs are "educational" within the meaning of section 501(c)(3) and the underlying regulations because they improve and develop the skills of professionals within the Q industry.

Concerning M's Off-Site Programs, all such programs are conducted in the same manner and offer the attendees the opportunity to improve and develop their Q professional skills. Off-Site Programs further M's exempt purpose of educating Q industry professionals in much the same way that M's On-Site Programs achieve their educational goals. M's Off-Site Programs typically reach larger audiences than the On-Site Programs, and the greater number of attendees makes for a wider range of discussion and debate. This, in turn, enables M to access more information for its public programs. Thus, M's programs serve a public rather than a private interest, and any benefit to the host organization resulting from these programs is merely incidental to the accomplishment of M's exempt purpose. See section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

Accordingly, M's tailored programs, both on-site and off-site, as described above, are consistent with the requirements under section 501(c)(3) of the Code. Also, the fact that some of these programs are conducted in foreign countries does not in any way jeopardize M's tax exempt status under section 501(c)(3). See Rev. Ruls. 71-460 and 74-16, both cited above.

Organizations like M, which are described in section 501(c)(3) of the Code, are subject to tax on their unrelated business income under section 511. In order for M's income to be subject to the unrelated business income tax, three requirements must be met: (1) the income must be from a trade or business; (2) the trade or business must be regularly carried on; and (3) the conduct of the trade or business must not be substantially related to M's exempt purpose or function. See section 1.513-1(a) of the regulations. As noted above, M's On-Site and Off-Site Programs are "charitable" under section 1.501(c)(3)-1(d)(2) and "educational" under section 1.501(c)(3)-1(d)(3). In accordance with section 513, M's programs are substantially related to its charitable and educational purposes, and as such, these programs "contribute importantly" to the accomplishment of M's exempt purposes. See section 1.513-1(d)(2). Accordingly, M's programs do not constitute an unrelated trade or business under section 513 and are not subject to tax under section 511.

RULINGS

1. The tailored programming, both on-site and off-site, as described above, is a charitable and educational activity, and, as such, does not jeopardize M's tax exempt status under section 501(c)(3) of the Code.

2. The income derived from the activities described above is related to M's exempt purposes, and, as such, will not result in the imposition of the unrelated business income tax under section 511.

This ruling is based on the understanding that there will be no material changes in the facts upon which it is based. Any changes that may have a bearing upon M's tax status should be reported to the Tax Exempt and Government Entities (TE/GE) Customer Service Office.

The mailing address is: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508,
The telephone number there is

We are sending a copy of this ruling to the E/GE Customer Service Office. Because this letter could help resolve any questions about M's tax status, you should keep it with your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Thank you for your cooperation.

Sincerely,

Gerald V. Sack

Gerald V. Sack
Manager, Exempt Organizations
Technical Group 4